RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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April 22, 1987 **LETTER 963**

THE MARKET: Milestones: On April 6 the D-J Industrial Average closed at a record high of 2405.54 confirmed with a record Transport high of 961.48. Subsequent Action: From the April 6 highs, the Averages turned down sharply, Industrials losing 152 points by April 14. Question: Can the Averages summon the strength to climb above their April 6 highs again? There is no time limit on their actions, but ultimately the Averages will have to better the April 6 highs. And if they can't? If they can't, Wall Street will find itself watching a primary bear market. As I have so often written, "The story is in the Averages."

THE PICTURE: Over the last few weeks the dollar has been running the markets. The continuing collapse in the dollar finally upset the bond market, and on April 14 the yields on the bellwether long-term Treasury bonds surged into the 8.5% area. With stock yields already reduced to unattractive levels seen only at major tops, the last thing in the world the stock market needed was a surge in interest rates. In the face of rising bonds yields, the stock market headed for lower levels.

I've been warning of coming trouble in Letter after Letter. I have discussed why this market is overvalued on an historical basis and overvalued compared with bonds (on a yield basis). I've also shown how this market is overextended in both duration and extent.

The actual statistics are rather fascinating. The Dow hit its high on April 6. Thus, the Dow rose from its July 1984 low to its 1987 high, a span of 33 months, without so much as a 10% correction. In all history there has been only one other advance that has lasted for better than 33 months without a 10% correction. That was the 34-month rise of 1962 to 1965.

So much for duration. How about extent? From its 1984 low of 1086.57 the Dow advanced to its April high of 2405.54 without so much as a 10% correction. That represents an uncorrected advance of 121%. This is a performance never seen before in stock market history. In fact, the nearest thing to it was the Dow surge from March to July 1933, a rise which advanced the Dow 96% without so much as an intervening 10% correction.

So what we have seen over the past few years is the greatest uncorrected advance in EXTENT in stock market history. We have also seen the second greatest advance in DURATION in stock market history.

We have also witnessed a market that is as OVERVALUED as any in stock market history. For instance, in March the S&P 500 Composite sold for 34.4 times its dividends. In Letter 960 (page 2) I published a chart showing that there have only been seven previous instances in which the S&P sold at 32 or more times its dividends. Four of these instances (1929, 1937, 1968, 1973) were followed by major bear markets, and the other three (1933, 1962, 1968) were followed by vicious corrections.

Finally, we have the Dow in the throes of an exponential rise, as illustrated in Letter 961. The Dow is now in the stage where it is (or has been) rising vertically, and of course this is the most exciting stage and also the most dangerous stage. Why exciting? Because straight up is always exciting. Why dangerous? Because as a rule once the price movement surges to an exponential spearpoint top, it can drop as rapidly as it rose (remember gold after the 1980 exponential spike!).

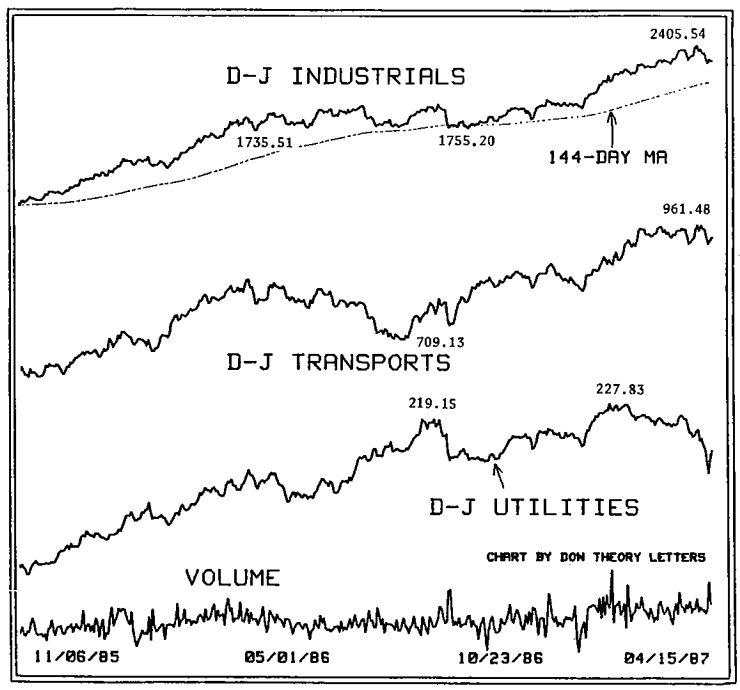
April 10 DJIA 2338.78; PTI 2586; A-D Ratio -4.71
April 16 DJIA 2275.99; PTI 2576; A-D Ratio -5.38

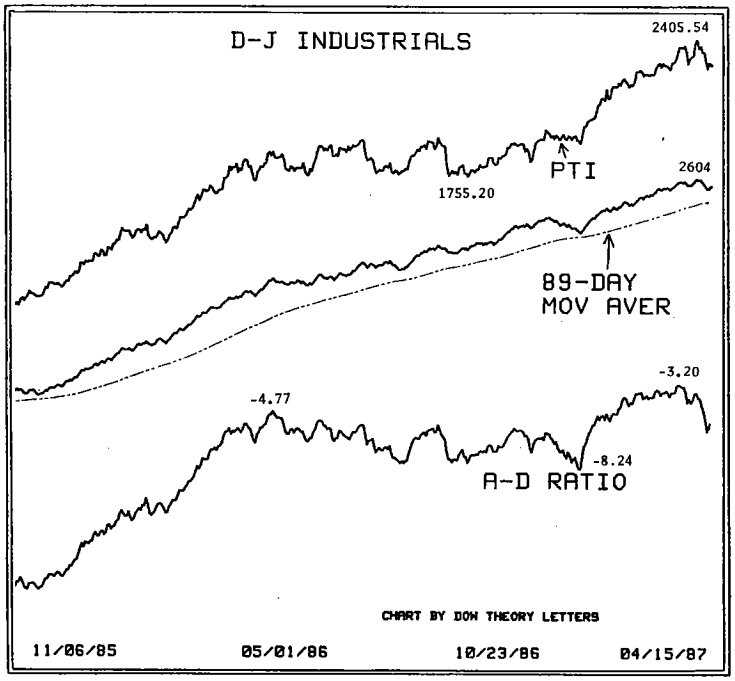
The basic point I want to make is this: The market action during the 1984-87 rise has in many ways been unprecedented. We might say that today's stock market has rocketed up into the realm of the unknown. We also know that stocks are pushing against a number of barriers that, in the past, have spelled trouble. And that is why I have been recommending: (1) extreme caution, (2) cessation of stock purchases, (3) a policy of profit-taking in stocks -- all stocks, including utilities.

Question: Russell, your PTI is still above its moving average. Furthermore, we have not yet received a Dow Theory bear signal. So why be so cautious?

Answer: First, there's nothing in Dow Theory that even remotely suggests that we wait for a bear signal before selling. No, according to Dow Theory, we sell stocks when they no longer represent values. In my opinion, we've been there during the last few months, and that's why I've recommended selling.

Secondly, a principle of physics states that for every action, there's an equal but opposite reaction. We have witnessed a record-breaking advance. The advance has been almost straight-line, and it has been uncorrected. In view of this, there is at least a fair probability that this market could also turn down in an unexpected and unorthodox way. And there is a fair probability that once the market turns down, it is going to go down in a way that is going to take a lot of investors with it.





I've written this before, but I think this is a good time to repeat it. A bull market likes to advance while taking as FEW people with it as possible (the majority usually join the bull market at or near the top). Conversely, a bear market likes to go down while taking the GREATEST number of people with it (the majority usually dump their stocks at or near the bottom).

The current bull market came a long way (in fact, it reached the extreme overvaluation area) before it started sucking in an eager public. So it would be entirely logical that the market could also turn down in such a way as to take a huge number of starry-eyed investors with it.

And I ask myself, "How could that happen?" The answer, it seems to me, is either (1) through a crash or (2) by the market declining very innocently and deceptively at first, with the decline accelerating into a costly smash as time passes.

Let me put it another way. We know that during the course of a COMPLETE bull and bear market cycle very FEW people are destined to make money. The majority of investors simply do not make money in the stock market. Yet, almost everyone who has bought and held stocks through this bull market must now show a profit. And that's not meant to be -- it's simply not the way the stock market works.

So my very cynical thought is that somewhere ahead, something has to occur which will PART THE MAJORITY of market participants from their money. It's going to happen as sure as the sun rises in the east and sets in the west.

My conclusion is that today, in this rarefied atmosphere, in a market that is stretched thin and uncorrected, in a market with high multiples and low yields, it makes perfect sense to be extremely careful. Being careful at this stage of the game means nailing down profits at an accelerating pace as the market climbs higher.

Question: Russell, won't your work provide at least hints of trouble prior to a possible top?

Answer: I believe so, and I certainly hope so. But there's one thought that has been on my mind. When I called the beginning of this great bull market in December 1974, there wasn't widespread interest in technical analysis. In fact, almost no one noted that the Transportation Average had failed to confirm the Industrials during the final plunge of the market. Furthermore, in late-1974 few analysts were talking about the fat yield on the Dow and the even fatter yields on the great majority of stocks (in fact, most analysts were openly talking about Dow 250 or 350).

But today the story is reversed. Technical analysts are a dime a dozen, and non-confirmations in the Averages are announced on the radio, on nightly TV programs, and in brokerage bulletins. Therefore, I feel that the ultimate market top (if we have not already seen it) is going to be very DECEPTIVE. It may sneak in with few if any technical "signals." It could even come in the guise of a final confirmation as all the major averages push to a final high. Remember this: In every bull market there must be a confirmation which will be the LAST upside confirmation prior to the next bear market.

Major tops in the market always come in a manner calculated to fool the vast majority of amateurs and professionals. And as a rule, the popular market techniques of the day will FAIL to identify the top when it arrives.

INVESTMENT POSITION: Changes in the primary direction of the market are few and far between. In other words, they are rare. But sooner or later every bull market in history has given birth to a bear market, and ultimately every bear market exhausts itself and a new bull market is born.

There isn't a man or woman alive who knows with certainty whether the April 6 peaks represented THE HIGHS for this bull market. We will only know with the passage of time. But with the overvaluation in stocks, with the surge in gold and gold shares, with the rise in interest rates, and the drop in bonds, I'm not at all sorry that I have been advising a policy of "taking profits in stocks."

Personally, I've sold a good chunk of my own common stock holdings, and if the Averages turn around and go to new highs (thereby reconfirming the bull market), I'll probably let them go up from there without me. I've played fun and games with this bull market for enough years now, and I guess I need a rest.

Nevertheless, in the absence of proof of any bear market, I'm keeping our one-horned bull in the box. Can he "revive" and grow back that other horn? I doubt it.

GOLD, SILVER, THE SECRET STORY: Ever since mid-1985 I have focused my subscribers' attentions on the precious metals and the slowly-building bull market in gold. As subscribers know, the price of gold hit a low of 284.25 in February 1985. From there it rallied, then backed and filled while building an impressive base. At around 325 I felt that the gold picture looked strong enough for me to state that a new gold bull market was in force.

Interest in gold in late-1985 was almost non-existent. I therefore found it necessary to repeat in Letter after Letter that gold was in a new bull market and that my subscribers should start accumulating gold on a regular monthly basis.

Since the start of the gold bull market in February 1985, bullion has risen roughly 55% in price while the gold and silver stocks have, since their mid-1986 lows, gone wild. But the remarkable thing is that the public (and perhaps 90% of the professionals and market advisers) has been totally blind to the new gold bull market. In fact, I can truthfully say that I have never, in my 40 years of experience in the markets, seen a comparable move that was so totally IGNORED by the public and by Wall Street.

I am taking up a larger than usual part of this report with the precious metals picture. I am doing this for two reasons. (1) I want to direct my subscribers' attention again to the precious metals area, and (2) I want to discuss some of the implications of the bull market in gold and silver and in the gold/silver stocks.

First, let's talk about what is happening today. For one thing, our federal debt is now over $2 trillion. Second, our gross national debt (debt of all kinds) is estimated to be around $8 trillion. This is an immense amount of debt for any nation to attempt to carry, and, of course, this debt is compounding day by day. Third, the US is now the world's largest debtor nation, and our trade balance continues to run an astounding $150 to $170 billion in the red.

Finally, we have a weakened president, a president who has lost credibility and now appears battered and disoriented. He was badly defeated on his veto of the highway bill, and it is questionable whether his own party will back him in the future (assuming he produces anything that is worth backing).

With America's love affair with Reagan waning, the odds now point increasingly to the next president being a Democrat. Furthermore, if one is to believe what one reads in the newspapers, leading Democrats are fairly chafing at the bit to raise taxes (particularly at the high end of the income scale) and to further increase domestic spending. Meanwhile, the dollar is swooning, and foreigners are wondering whether the US may not be the next "sick man" of the Western world.

What does all this mean? It means that the US is now in the precarious position of having to do one of the following: (1) tighten its belt, possibly to the point of recession, or (2) have recession thrust upon it (via collapsing markets and higher interest rates) or (3) opt for inflation.

I am including below part of a particularly penetrating editorial from the April 20 issue of Business Week. Please read the piece carefully:

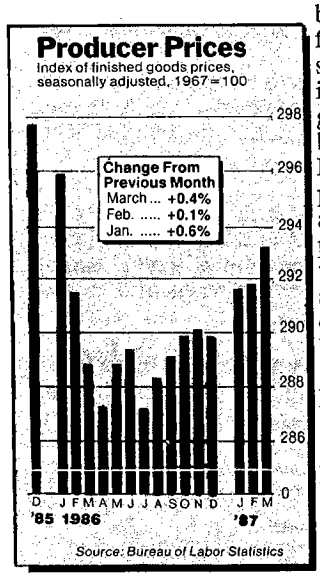
It's a grim choice: During the next decade or so, the U. S. must either grow faster or live on less. U. S. economic growth has slipped from the expansive 4%-a-year level of the 1960s to a sluggish 2.4% last year. But while that was taking place, did Americans start consuming less and saving more? Not at all. Instead, they decided to buy now and pay later. The money they borrowed from themselves, and, increasingly, from foreigners, went not into productive investments that could increase national output and wealth but into maintaining a standard of living the country could no longer afford. Today's budget and trade deficits are just a quick summary of this long borrowing binge. Meantime, while Americans lived beyond their means, foreign producers forged ahead, outpacing U. S. firms not only with lower-cost labor but also with sophisticated manufacturing expertise. The sad but predictable outcome is that the U. S. now finds itself carrying an unprecedented debt burden exactly at a time when it is losing competitive ability to produce the goods and services it must sell to meet its bills.

There is a way out: to increase productivity growth, now stuck at about 1% a year. But this will be extraordinarily hard to do. The key lies in regaining manufacturing leadership—or at least equality. It will require wrenching, far-reaching changes across the full range of manufacturing operations, from plant floor to executive suite.

In the face of all this, the dollar has been collapsing -- collapsing despite efforts on the part of our European allies and Japan ("the Group of Seven") to "stabilize" the dollar (which I now believe is actually undervalued in terms of purchasing power).

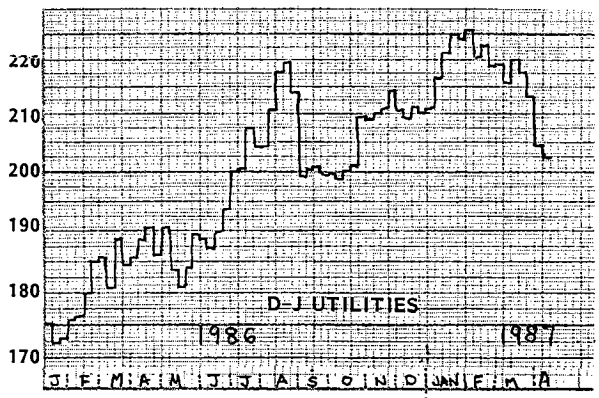
In the last Letter I stated that US and world debt is so huge and is piling up at such a fantastic rate that the only outcome can be (1) outright repudiation (or repudiation in a more subtle form such as "extension" or "renegotiating") or (2) inflation.

So far, the US has chosen the path of monetary inflation. The Fed has, for the past 27 months, flooded the money markets at double digit rates. Up to very recently, this ocean of new credit has not been visible to the average American because prices of things have been held down due to vicious foreign competition. But with the slide in the dollar and the subsequent increase in the price of imported goods, the signs of price inflation are beginning to appear. In fact, the Labor Dept. last week noted that producer prices are now moving up at a 4% rate and this rate will shortly be passed on to consumers. Last week the NY Times published this chart, and the trend is clear. As you can see on the chart, the trend of inflation has been UP ever since March 1986.

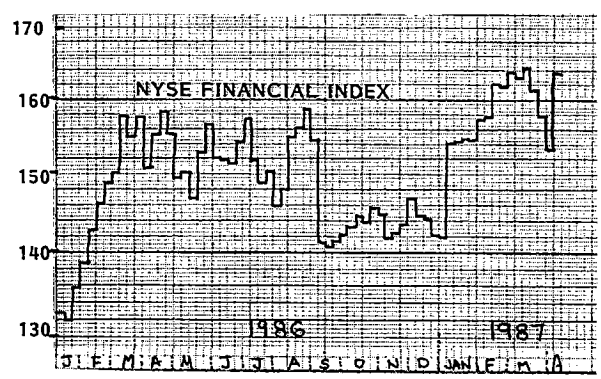


My own charts tell the story only too well, and I am including a number of these weekly ratio charts in this Letter. All the charts are based on price action during 1986 and 1987 to date (weekly closings), and all the charts are drawn to the same ratio scale so that the various price movements can be CORRECTLY COMPARED. So let's discuss what we see on these charts.

(1) The D-J Utility Average topped out on January 22 at 227.83 I have stated repeatedly that the Utility Average can act as a market bellwether. Utilities are sensitive to interest rates, corporate and consumer power consumption, and the whims of the regulatory authorities. The top–out of the Utility Average on January 22 should serve as a warning that something unhealthy is occurring in the stock market.



(2) The NYSE Financial Index contains ALL the financially-oriented issues on the NYSE, including brokerage stocks, banks, fund mangement issues, S&Ls, and small loan companies. The Financial Index is now struggling to hold above the six peaks (count 'em!) that were formed during 1986. This is a key indicator and is worth watching closely.

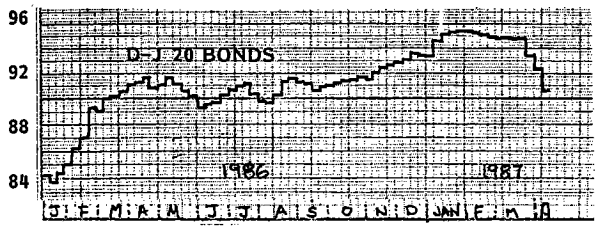


(3) The D-J 20 Bond Average has topped out -- at least temporarily. This obviously spells higher interest rates, and already the T-bonds are into the over-8% yield area, and mortgage rates are pushing higher. If the economy slows down, the Fed will probably

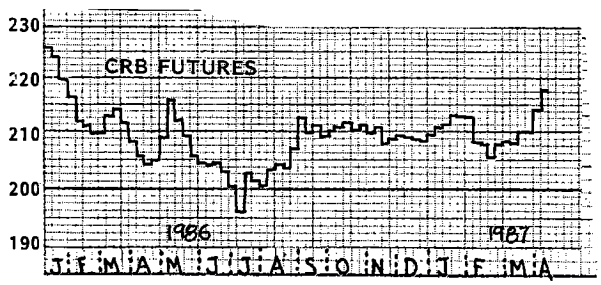
try to get Japan and our European allies to bring down their bank rates. This may or may not work. But it could be a stabilizing force for the bond market in the future. Nevertheless, the trend of bonds is now down.

Don't blame world interest rate trends for the top-out in the US bond market, blame the sagging dollar. As I said in the last Letter, foreigners have been buying roughly one-third of the US deficits (US Treasury bills, notes, and bonds), and in terms of their own currencies they have been getting KILLED.

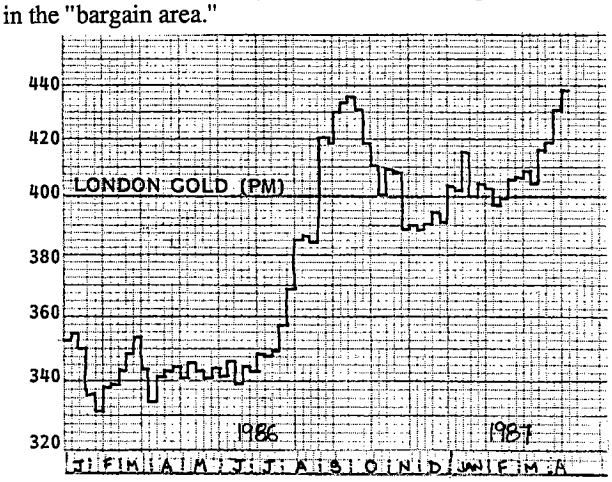
Last week the yields on the Bond Buyer's Muni Bond Index rose to 8.68%, actually above the 8.45% yield on long-term taxable T-bonds. Thus the munis are now as over-sold as I have ever seen them.



(4) The CRB Commodities Futures Index hit 217 last week, and as you can see on the chart this index of 27 different commodity futures now presents a bullish pattern. The meaning here is that for the first time in a year commodity prices are heating up -- a prelude to price inflation.



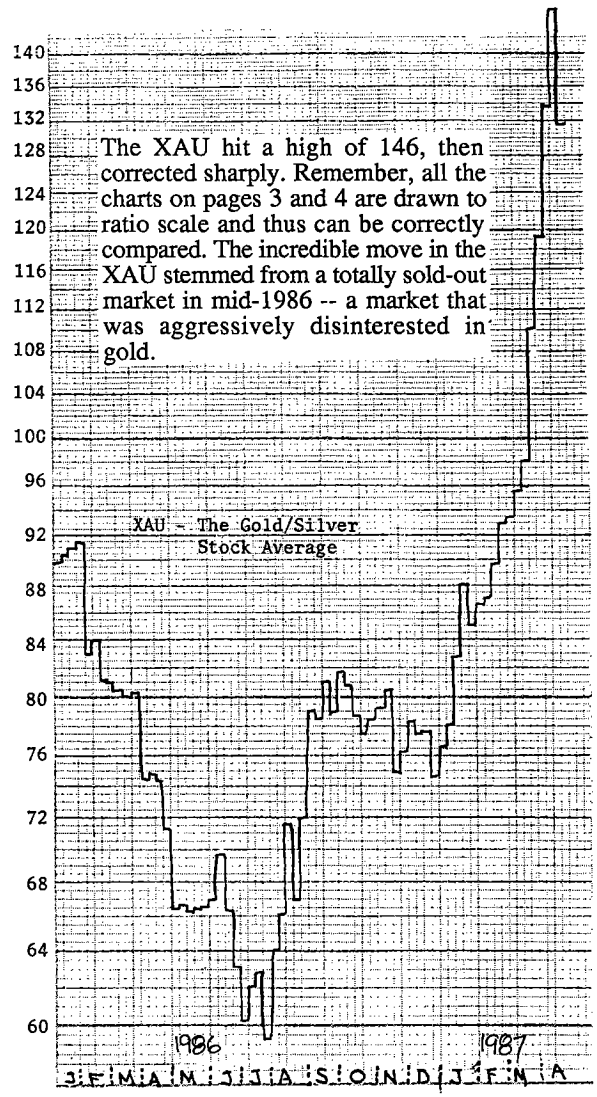
(5) The gold chart (the metal) is in a strong bull trend, and last week's rise above 440 constitutes a powerful breakout signal. I have stated repeatedly that the gold bull market is still young. As far as the metal is concerned, I have written that gold below 400 was in the "bargain area."



(6) One of the fascinating gold stories is being told by the XAU gold/silver average. The rise since the low of 59, set last July, has to be one of the most spectacular moves in a group of stocks in Wall Street history. Last week the XAU hit a price of 146, a rise so far of 147% in less than a year! You would have had to have hung around the boardrooms a long time to see anything resembling this baby.

My own feeling is that the gold share price structure is way over-extended. Therefore a correction (even a severe one) should not come as a surprise. Some of the P/Es on the mining shares have risen out of sight: 88 on Homestake; 51 on Lac Minerals; 594 on Callahan; 75 on Echo Bay; 68 on Battle Mountain; 47 on Campbell Red Lake; 114 on St. Joseph Gold; 58 on Freeport McMoran, and 40 on Newmont Mining.

Back in January I recommended purchase of the Lexington Goldfund just above the breakout at 4. Last week that fund pushed well over 7, a phenomenal rise for a no-load fund in just over three months! (Chart courtesy of Growth Fund Guide, Box 6600, Rapid City SD 57709.)



The XAU hit a high of 146, then corrected sharply. Remember, all the charts on pages 3 and 4 are drawn to ratio scale and thus can be correctly compared. The incredible move in the XAU stemmed from a totally sold-out market in mid-1986 -- a market that was aggressively disinterested in gold.

NOTES & QUOTES: The great challenge facing Russia today is the "information revolution." I noted this many months ago when Russia finally bowed to the information age and brought computers into the schools. Gorbachev knows it and so do many Soviet leaders -- either Russia moves into the computer and information age, or it drops behind the rest of the world like a decrepit dinosaur.

But the danger of open information is already becoming apparent. A video is being secretly distributed throughout Russia which shows Gorbachev's wife, Raisa, indulging in lavish spending and dressing in expensive fashions. One rumor is that the KGB was instrumental in distributing the film.

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In Zimbabwe (formerly Rhodesia) the whites are uneasy. Ian Smith (a white leader and former prime minister of Rhodesia) has been suspended from parliament. More ominous, senior Zimbabwean ministers now want to change the country's constitution to eliminate all whites from parliament. Naturally, South Africa's whites are watching with great interest.

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The Japanese continue to buy up the Hawaiian Islands. Japanese investors have bought up 2,900 acres on Oahu's North Shore and

have started developing a $2-billion, eight-hotel, mega-resort on Oahu's west beach. Last year 1 million Japanese visited the Hawaiian Islands, one-third of them on honeymoons. Item: Today the Japanese can buy a US dollar for approximately 140 yen, 45% LESS than two years ago.

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Texaco's lead law firm, Cravath, Swaine & Moore, didn't choose bankruptcy for TX lightly. The law firm is a $1 million creditor of TX's. TX's legal and advisory fees are now running at the rate of $1 million a week!

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You must have seen at least one of the "nothing down" real estate promoters on TV. Up to a few months ago, these touts were all over the airways, telling you how you could make a fortune starting with zero dollars. Well, trouble has zapped most of the nothing-downers. Ed Beckley, who sold his "$299 Millionaire Maker", has filed for bankruptcy (he was deluged with 4,000 refund requests). Companies promoting Tony Hoffman and best-selling author Albert Lowry have closed. At last estimate, 17,000 people nationwide want refunds from the gurus and the gurus' creditors are owed million of dollars.

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The Population Crisis Committee (PCC) lists the world's nations in terms of a "human suffering index" from the best to the worst. The top 10 (best) are (1) Switzerland, (2) West Germany, (3) Luxemburg, (4) Netherlands, (5) US, (6) Belgium, (7) Canada, (8) Austria, (9) Denmark, (10) Japan. The 10 worst are (1) Mozambique, (2) Angola, (3) Afghanistan, (4) Chad, (5) Mali, (6) Ghana, (7) Somalia, (8) Niger, (9) Burkina Faso, (10) Central African Republic, the worst.

* *

My father was a civil engineer. He loved building, and that's what he did during the years prior to 1929. When the Depression hit, construction literally ended, and my father then went into management. He once told me, "Dick, the good thing about a boom is that it gets the buildings up. Real estate operators always overdo it during a boom, but the buildings do get built. Then, when the inevitable collapse comes, the builders go broke, but the buildings continue to stand. That's the good thing about a building boom. Things do get built."

I thought of my father's words as I read about the auctions going on in Denver. On March 5 a Denver developer (Denver has the nation's most over-built downtown market) auctioned off 200,000 square feet of space in nine office buildings at starting bids of $1 to $4 a foot. Five to six years ago the same kind of space hit a high of $32 per square foot.

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The US mint turned out 9.4 billion pennies last year. Yet the Treasury estimates that 6 billion pennies disappear each year. Where do those lowly pennies go? Nobody's sure -- some pennies go to the bottom of wells, some are re-stamped into washers, some are thrown away, some are used for ear rings, on and on. Why is the penny still in use? Proponents say that if the penny was eliminated, it would cost consumers millions in extra taxes as the nickel would then be used for sales tax purposes. The penny is also a symbol for politicians. If the penny was eliminated, anti-inflationists could claim that our lowest denominated coin had been inflated out of existence.

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There's no substitute for using your instincts, your common sense, and your brains. I don't care whether you're buying a house, picking a physician or choosing a car. Case in point: The Thomases from Boise inherited $800,000, and their conservative portfolio yielded $45 to $60 thousand a year. Then they went to Merrill Lynch, putting down $600,000 for investing. Their broker told them their portfolio was for "little old ladies." They then went into commodities, stock options, and other stocks. Their losses in commods were $178,000, their losses in options in stocks were $115,000.

The Thomases sued, and before a National Assoc. of Securities Dealers arbitration board they were awarded $175,000. Merrill called it an "outrageous decision" and is appealing the award. But to my mind, the Thomases made an outrageous decision when they moved into an area they knew nothing about. When asked why they did it, the Thomases said,"because it was Merrill Lynch. We trusted them. It was like dealing with your local bank. And besides, they led us to believe it was in our best interest."

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As veteran readers know, I have for years followed the exploits of Warren Buffet, the fabled investor from Omaha (personal assets $1.4 billion). Buffet runs Berkshire-Hathaway and owns 41% of the stock. In his latest report Buffet notes that he is not excited about either stocks or bonds, and he has put some of his money into arbitrage situations (which he simply calls "workout" situations). Buffet, a value expert, states that he hasn't found any new stocks "that come close to meeting our tests." Buffet notes that stock prices have become "gloriously uncoupled from the plodding performances of the businesses themselves," and of course, I have been writing about this for months (via overvaluation). As a place to park new money, Buffet has chosen tax-exempt bonds.

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From our "Amazing Women" Dept: Jan Goodwin, executive editor of the Ladies' Home Journal, is out with a book entitled "Caught in the Crossfire" (Dutton, $18.95). Goodwin spent three months (would you believe?) in Afghanistan disguised as an Afghan man. She followed the Afghan freedom fighers, crossing 10 of the country's 29 provinces. Goodwin was furious at the Soviets because of their disgusting war methods (for instance, toys that explode in childrens' hands). States Goodwin, "With Pol Pot, with Hitler, with Idi Amin, we were told it was the work of a madman. With the Kremlin, it is not one man and we must assume they are not mad. I am not anti-Soviet. What I am is anti-atrocity, and I don't care who is perpetrating those atrocities." Goodwin is being invited to speak before Congress on the war in Afghanistan.

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I voted for Reagan, yes, I did. But do you get the feeling that the Reagan Administration is totally "at sea" as far as the domestic economy is concerned, as far as the international situation is concerned, and as far as the military is concerned? In other words, I get the uneasy feeling that the Reagan administration is a ship without a rudder.

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From our "Milestones in Hypocrisy" Dept: (1) After stupidly allowing the Russians to build the new US embassy in Moscow, US diplomats claimed that the building was unusable because it resembled one huge microphone ("bugs" were planted everywhere). Whereupon, the Russians immediately held a news conference in their own Washington embassy and showed reporters bugs that they claimed the US had planted in the Russian embassy. The New York Times claimed that the Russian counter-attack was not without its "comic" aspects.

(2) After signing a treaty which practically eliminated whale hunting, Japan has announced that this year it will kill 875 whales for scientific study -- and then sell the carcasses because they will have no further use for them.

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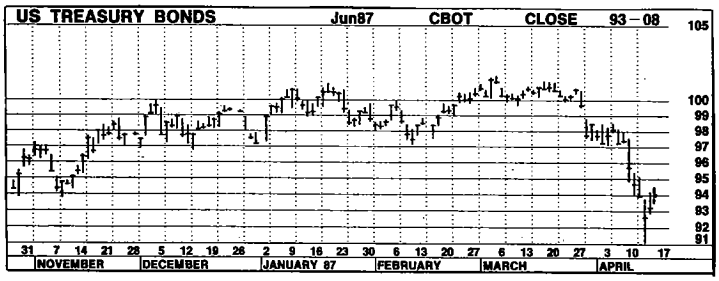
Last week Japan's stock market became the biggest (in capitalization) in the world, finally surpassing the American stock market. The "transfer" of power came partly through weakness in the dollar. Based on capitalization (number of issues times their values), the Japanese stock market was worth $2.688 trillion while the US market was worth $2.672 trillion. Volume on the Tokyo exchange, by the way, frequently goes over 1 billion shares per day.

BONDS, MONEY, RATES: Investors buy bonds using two broad methods. One way is to buy bonds and just keep buying them -- on the upside and on the downside. If the bonds go down in price, you're buying bonds with higher coupons, and they will compound at much higher rates. If the bonds go up, then your assets are increasing. The other way is to buy bonds when they look cheap and sell them when they look expensive. This method

requires timing, while the first method requires discipline, patience, and an understanding of compounding.

Last week the bonds took a big pounding as the dollar weakened and as bondholders panicked. The June T-bond contract shows the swoon that hit the market. Support came in at 91, and it looks to me as though that was at least a temporary bottom. The muni bonds suffered from a lot of switching and dumping on the part of the muni bond funds, and it was a classic case of illiquidity. By April 15 I thought the better-grade munis were providing yield bargains compared with the T-bonds. In general, all areas of the bond market appeared oversold and ready to rally.



NOTES ON COINS & COLLECTIBLES: Rare coins? Salomon Bros. lists them as the single most profitable investment of the last 10 years, having appreciated (according to Salomon) at a compound rate of 15.1% a year between 1977 and 1986. Maybe so, but here's the experience of a friend of mine. He bought a good set of the silver commemoratives, the so-called "short set" which consists of 50 different silver coins. At the time his coins were graded mostly MS-60 to MS-65, and he paid $20,000 for the set in 1980.

Last week he took the set to a very honest local dealer. He wanted to sell the set. The dealer told him, "I'll check it out and see what I can do." A few days later the dealer called, "I took it to three different parties. No one's interested. Times have changed since you bought these coins. To sell them today, they've got to be sent out to be graded, and grading is much tougher now than it was when you bought these coins. A coin you bought as MS-65 back in '81 might be an MS-60 today. So it will cost you about $25 a coin to grade these or $750 for your 30 best coins. The other 20 coins are lower priced and not even worth grading."

"How much do you think I can get for the whole set once they are graded?" my friend asked.

The dealer said, "Maybe $13,000 or $14,000. You see coins, all except the top-graded gold pieces, have come down in price over the last six months. And the market for the silver commemoratives has been very sloppy." So much for rare coins.

And in case you've wondered, the market for "investment quality" stamps has really been rotten. Stamps have only recently begun a mild recovery from their collapse following the 1980 highs.

Russell advice: If you're a serous collector, sure, have fun buying coins and stamps any time, any month, any year. But if you're an investor, buy your stamps and coins during a depression and sell 'em during a boom (and by the way, we're not in a depression now).

If you think buying stamps or coins is tough, they're a picnic compared with buying precious gems and diamonds. It's axiomatic: You can't buy diamonds right from a retail or a chain jewelry store. Well, you might conceivably be able to if you happen to be an expert on cut, color, clarity, defects, carat weight, etc. Assuming you're not a gem expert, the next best thing is to go to an honest jeweler and let him buy your stone for you. And don't buy your stone without a G.I.A. certificate, which will at least tell you the quality of your stone (the G.I.A appraisal will not represent the potential sale price, it will simply be a reference price somewhere near the retail value).

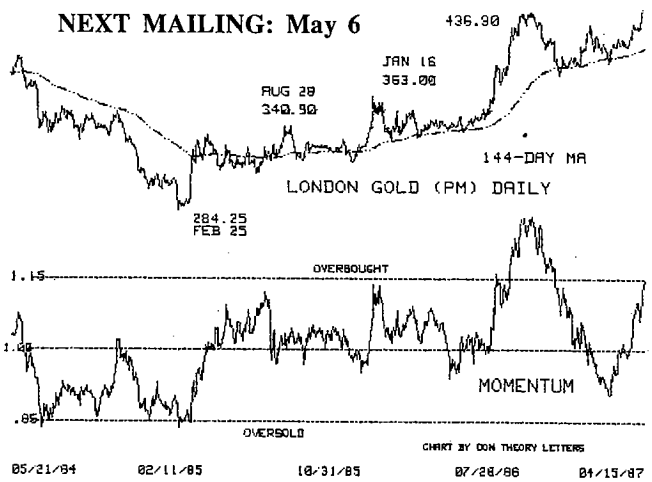
But don't get me wrong. I love diamonds, I love the modern brilliant cuts, I love diamonds as jewelry, and I think a beautiful, large diamond (above 3 carats) bought right, is not a bad long-term investment (furthermore, there are very few investments that will give your wife as much pleasure as an outstanding diamond). Diamond prices were on the floor in 1984, but they're moving up now.

Many buyers of gold bullion-type coins write to tell me that they are worried about counterfeits. In general, this should not be a big worry. If gold coins are counterfeited, such fakes are usually confined to rare or antique coins -- coins that can be cast. Modern bullion gold coins such as krugerrands, eagles, maple leafs, etc. are not cast: they are die stamped. The presses which stamp out these coins cost millions of dollars and die stamped coins are turned out under tens of thousands of pounds of pressure.

Nevertheless, there is a very clever little item available which will immediately and easily identify any fake or part-gold or tampered coin. The little machine checks the coin for diameter, thickness, and specific gravity. If your coin checks out for all three then it's GOLD (the test takes about seven seconds). The handy little gadget is manufactured by Fisch Instruments, Box 160332, Sacramento, CA 95816. If you're are a steady coin buyer as I have recommended you be (and as I am), it's not a bad idea to have one of these valuable little "testers." Write to Fisch for details.

MORE ON GOLD: I've written a lot on precious metals in this Letter, but a lot's been happening lately in the precious metals area. The accompanying chart updates the gold action. Back in February 1985 gold surged above its 144-day moving average, and it has been walking along (or above) the MA ever since. Furthermore, the MA has been rising since February '85, and this action alone has kept us bullish on gold.

Gold momentum (i.e., gold's 89-day rate-of-change) has now moved to the edge of the overbought zone, and thus gold may back off and consolidate for a while. However, the rise in London spot gold to 440 (see point & figure chart in the last Letter) was a major upside breakout. Gold, according to my P & F chart, has now built a base big enough to take it well into the 500 area.



LATE NOTES: One late note is that Faye and I are off to New Orleans for two days and then six days in NYC. But don't worry; all the charts go with us.

The stock market is on the rebound from the April 14 lows. You might watch the daily WSJ chart for a potential head & shoulders top formation in the Dow. But give the stock market its due. After a 152-point Dow drop in a matter of six trading days, it's certainly entitled to rally -- and maybe even try for the highs. And these are the highs: D-J Industrials 2405.54, D-J Transports 961.48. Also, the high for the S&P 500 was 301.95, the high for the NYSE Composite was 171.08. If it's a bull market all those highs should be bettered -- but in the market's own good time.